Supreme Court, U. S.
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IN THE

Supreme Court of the United States

October Term, 1977

No. 77-96

BRITISH AMERICAN COMMODITY OPTIONS CORP. and LLOYD, CARR & Co.,

Petitioners,

—against—

WILLIAM T. BAGLEY, Chairman of the COMMODITY FUTURES TRADING COMMISSION; JOHN V. RAINBOLT III, Vice Chairman of the COMMODITY FUTURES TRADING COMMISSION; READ P. DUNN, GARY SEEVERS, and ROBERT L. MARTIN, Commissioners of the COMMODITY FUTURES TRADING COMMISSION,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONER'S REPLY BRIEF

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British American Commodity Options Corp.
and Lloyd, Carr & Co.,

Petitioners,

—against—

William T. Bagley, Chairman of the Commodity Futures Trading Commission; John V. Rainbolt III, Vice Chairman of the Commodity Futures Trading Commission; Read P. Dunn, Gary Seevers, and Robert L. Martin, Commissioners of the Commodity Futures Trading Commission,

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REPLY BRIEF OF PETITIONER BRITISH AMERICAN COMMODITY OPTIONS CORP.

Set forth below is the Reply Brief of Petitioner, British American Commodity Options Corp. ("British American") in support of its prayer that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit entered on April 4, 1977, as amended on May 11, 1977.

(1) The Respondents do not dispute any of the reasons for granting a writ of certiorari set forth in the Petition ex-

cept (i) as to double segregation which they misrepresent as a traditional regulatory measure and (ii) as to the validity of the registration provisions where they attempt to distort Petitioners' position as a subjective objection based upon their particular situation rather than an objection based upon a fundamental flaw in the legislative and regulatory provisions themselves raised at the outset of this litigation two months prior to the effective date of the registration provisions and prior to the retaliatory measures of the CFTC against the two dealers who instituted this litigation.

The Respondents further contend that these matters should not be reviewed (i) since there is no conflict with any decision of this Court (this concededly is the first case to be presented to this Court with respect to a novel and confiscatory regulatory scheme adopted by this newly created agency) and no conflict among Circuit Courts (concededly the Second Circuit's decision is the only Circuit Court decision with respect to these regulations). That there is ample and substantial disagreement among the lower courts is evident from the compendium of pending litigation chronicled in footnote 5 to Respondents' Brief.[1] As noted by Mr. Justice Marshall this is a rather "fact-intensive" question and it is significant that the great majority of the triers of fact subsequent to the decision of the Second Circuit Court have preliminarily enjoined double segregation.

(2) The Respondents contend that these regulations are not ripe for review because the CFTC intended them only

[1] We are advised by counsel for Frankland Commodities Corp. that at the time of its motion for a preliminary injunction it did not show irreparable injury since its application for financing was pending. The proposed financing subsequently was denied and we are unaware of any specialty dealer who has obtained the requisite financing.

as temporary measures to be subsequently amended and supplemented. The possibility of amendment or revision cannot and should not deprive Petitioner of its right to contest a regulatory scheme which if upheld will put all ethical specialty dealers out of business.[2] As noted by Mr. Justice Marshall in denying Respondents' motion to vacate the stay of mandate, double segregation "would fundamentally alter the ground rules for doing business in a substantial industry, with potentially fatal consequences for a number of the firms currently in the trade, and this case presents the first opportunity for this Court to pass on action taken by the recently created Commission". *Commodity Futures Trading Commission, et al.* v. *British American Commodity Options Corp., et al.,* [S. Ct. A-86 (77-96) August 8, 1977].

(3) The Respondents' Brief in Opposition continually refers to matters dehors the record. This is not only improper appellate practice but it is especially prejudicial in this case because the CFTC moved for summary judgment, thus closing the record. However, certain matters should be brought to this Court's attention.

(a) the inspections referred to at pages 10 and 11 of the Brief in Opposition fail to state (i) whether or not such firms are complying with "double segregation" or (ii) whether or not such firms are specialty commodity option dealers.[3]

[2] The only alternatives are naked options or very short term options, both of which are clearly contrary to the customers' interests.

[3] It is conceded that the extremely large and diversified securities broker-dealers and commodity futures dealers, who desire to dominate this business at the expense of the specialty dealers who developed this industry, whose commodity option business represents an insignificant portion of gross revenues will be able to finance double segregation out of their non-commodity option revenues.

(b) As to footnote 19, the undersigned has been advised that the customers of Palmer Trading Company, Inc. are being serviced through another dealer and that its financial problems arose not from financial instability but because of the embezzlement and unauthorized trading of a trusted employee.

(c) The registration application filed by Lloyd, Carr & Co. in January, 1977 was identical in all respects, except for the change in name, with the prior application in the name of Lloyd, Carr Financial Co. This change was made at the request of the staff. Lloyd, Carr had been duly registered as a commodity trading advisor and originally filed its application as an FCM on October 1, 1976. When the CFTC represented to the Second Circuit on January 17, 1977 that Lloyd, Carr had never filed counsel produced the time stamped copy of such registration application and the cancelled check representing payment of the requisite registration fee (A 702-708).

(d) Respondents completely misinterpret the affidavit of Leonard Goldstein dated July 5, 1977, filed with the Second Circuit Court which is part of the record before this Court relating to the motion to vacate the stay (No. A-86), which affidavit studiously avoids any reference to compliance with double segregation except to state that compliance with double segregation would place the intervenors at a competitive disadvantage.

(e) The reference to the pending administrative proceedings and injunctive actions described in footnote 8 is not only improper and prejudicial but totally inaccurate. In reality the CFTC took retaliatory measures against these two firms because as responsible

members of this industry they promptly sought pre-enforcement review of these regulations which radically changed the ground rules for doing business.

(4) The Brief in Opposition fails to address itself to the importance of resolving the constitutionality of a licensing regulation which permits a federal regulatory agency from forcing an existing firm out of business, an existing employee from earning a livelihood or preventing the entry of a new firm or employees into this field of commerce without any semblance of due process by (i) failing to process applications (i.e. Lloyd, Carr and thousands of existing employees presently in the industry) or (ii) by making allegations in an administrative complaint and then arbitrarily delaying the administrative proceeding (i.e. British American which filed its CTA application in March, 1976 which has not yet been ruled upon by the CFTC or its FCM application in December, 1976 which also has yet to be ruled upon.

This licensing regulation is not only unique but is clearly distinguishable from the licensing scheme of the Securities and Exchange Commission which sets forth standards, including an examination relating to the applicant's knowledge. Furthermore, under 15 U.S.C. §78o(b)(1)(B), an application must be acted upon within a specific time limit and any registration hearing must be held and concluded within 120 days of the filing of the application.

The CFTC in its Brief in Opposition for the first time takes the position that even though Petitioner's due process contentions may be valid they "should more appropriately be reviewed in any enforcement proceedings against them", which as stated above can be unduly and indefinitely delayed. If the licensing provisions and/or the CFTC's application thereof are unconstitutional it is appropriate for the Supreme Court to review this regulation which has and

will create a serious injustice to a number of firms and thousands of employees.

(5) The calculation of the net interest cost of double segregation propounded by Respondents is meaningless since it presupposes the ability of a specialty dealer to borrow. It is self-evident that since the customer's option cannot be pledged as collateral, financing is unavailable to specialty dealers. As to their discussion of the applicable bankruptcy principles not only are the cases on page 20 inapposite the CFTC has failed to take the necessary steps to obtain the clarifying legislation which its Advisory Committee recommended as a necessary condition precedent to adopting double segregation. Under existing bankruptcy laws it would appear that double segregation, if upheld, will not afford commodity option customers any additional protection.

(6) There is no assurance that the proposed new regulations discussed at page 13 of the Brief in Opposition will ever be adopted or that they are anything more than insurance against the invalidating of double segregation by this Court. By proposing to place the ultimate regulatory "responsibility" with entities, such as foreign exchanges, outside the jurisdiction of the American courts, the CFTC is attempting to immunize double segregation from further attack.

Other Issues Raised

(7) With respect to the other issues, the Respondents' Brief in Opposition is substantially similar to their brief before the Second Circuit and attempts to relitigate the merits rather than oppose the reasons propounded by Petitioners for granting a writ of certiorari.

CONCLUSION

For the foregoing reasons, as well as those urged in the Petition, a writ of certiorari should be granted.

Respectfully submitted,

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